Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Unbundled Access to Network Elements	)	WC Docket No. 04-313
	)	
Review of the Section 251 Unbundling Obligations Of Incumbent Local Exchange Carriers	)	CC Docket No. 01-338

REPLY COMMENTS OF THE PACE COALITION, BROADVIEW NETWORKS, GRANDE COMMUNICATIONS, AND TALK AMERICA INC.

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The Promoting Active Competition Everywhere ("PACE") Coalition, Broadview Networks, Grande Communications, and Talk America Inc. (collectively, the "Joint Commenters"), through their undersigned counsel, respectfully submit their reply comments to the Federal Communications Commission ("Commission") in the above-captioned proceeding.

I. EXECUTIVE SUMMARY

The record in this proceeding is replete with evidence that competitive local exchange carriers ("CLECs") serving the plain old telephone service ("POTS") market are impaired without access to unbundled local switching. Numerous state commissions submitted summaries of the records developed in their *Triennial Review Order* impairment dockets which prove that there is substantial impairment in the basic voice services market. Commenters warned the Commission that a loss of access to unbundled local switching will lead to an elimination of competitive alternatives in the POTS market due to the substantial economic and operational impairments CLECs continue to face when trying to serve residential and small business customers using competitively-provided switches.

The Bell Operating Companies ("BOCs") have not presented any evidence that CLECs are not impaired without access to unbundled local switching. In fact, the BOCs no

longer claim that existing unbundled network element-loop ("UNE-L") competition in the mass market demonstrates non-impairment for local switching (which it does not). The BOCs have replaced this argument with the claim that intermodal competition renders UNE-L based competition irrelevant. This shift is in response to the undeniable fact – as demonstrated by the evidence in the record – that CLECs remain impaired without access to unbundled local switching.

Yet intermodal alternatives, to the extent that they exist, do not override the impairment analysis for the POTS market. As the Joint Commenters demonstrated in their initial comments, and numerous commenters, including the state public utility commissions agreed, POTS service still constitutes a distinct market. POTS service is separate and distinct from – and cannot be substituted by – intermodal alternatives including wireless and voice over internet protocol ("VoIP"). In addition, in evaluating intermodal alternatives, the Commission must reject the approach that the New York Department of Public Service has proposed. That approach, which attempts to weight non-POTS alternatives to evaluate impairment, is arbitrary and capricious and bears no relationship to competitive market conditions.

Eliminating unbundled local switching will not trigger or facilitate UNE-L availability; the availability of unbundled local switching is not the root cause of the dearth of UNE-L competition. Indeed, TELRIC-based local switching rates do not discourage UNE-L competition. For this claim to be plausible, it would be necessary that local switching is priced below the CLEC's incremental cost of utilizing its own switch to provide POTS service. As the Joint Commenters discuss herein, there is no empirical or even theoretical data to support that claim.

The Commission must recognize that states have the authority to adopt their own unbundling obligations, and must reject the BOCs' efforts to remove authority from the states to promote local competition through the adoption of unbundling requirements. There is no merit to the BOCs' arguments that the states only have a consultative role in the section 271 process, and that a state's role ends when it makes a recommendation to the Commission regarding the BOC's application for in-region interLATA authority. Under the plain language of the Act and their own state statutes, state commissions have authority that extends beyond a consultative role, and it would be unlawful for the Commission to adopt – as the BOCs have suggested – a blanket rule prohibiting the states from exercising any regulation of network elements beyond that boundary.

If the Commission finds non-impairment, then it must require all carriers to comply with the terms and conditions of their interconnection agreements to effectuate the rule changes. The Commission must reject Verizon's attempt to unilaterally change the provisions in its interconnection agreements without first following the change of law processes specified in those agreements. There is no merit to Verizon's argument that a Commission finding of no impairment does not constitute a change of law, and all carriers must comply with the terms of their agreements.

II. POTS COMPETITION IS DEPENDENT ON UNE-P

The most remarkable aspect of the BOCs' comments is the claim they no longer emphasize – that is, the claim that existing UNE-L competition in the mass market demonstrates non-impairment for local switching. For all practical purposes, the BOCs have abandoned this theme, replacing it with the claim that *intermodal* competition renders UNE-L based competition irrelevant. Nothing could be further from the truth. As explained in the Joint Commenters'

initial comments,[1] the analog phone market remains a core element of the incumbent local exchange carrier ("ILEC") monopoly and is roughly the same size today (well in excess of 100 million lines) as it was when Congress passed the Telecommunications Act of 1996.[2] The Commission cannot ignore (as the BOCs would like) its *duty* to extend competition to the analog voice market, upon which the vast majority of residential and small business customers depend even today.

The BOCs' tactical shift to "the intermodal argument" is a response to the undeniable fact – first documented in state impairment proceedings and now admitted by the BOCs themselves – that UNE-L competition in the mass market is moribund. The dearth of UNE-L mass market competition is the direct result of the impairments that effectively deny entrants meaningful access to the ILEC loop monopoly: the hot cuts and backhaul needed to serve customers from a CLEC-provided switch.

Eliminating local switching will not reenergize UNE-L because it is not the availability of local switching that discourages UNE-L based entry. Indeed, the fact that CLECs will pay the relatively high unbundled network element ("UNE") rate to use the ILEC's switch – rather than incur the much lower incremental cost of excess capacity on CLEC switches – is an economic measure of the loop-related impairments that local switching overcomes.[3] When the

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1 *See Initial Comments of the PACE Coalition, Broadview Networks, Grande Communications, and Talk America Inc.*, WC Docket No. 04-313, CC Docket No. 01-338 at 42 (filed Oct. 4, 2004) ("PACE Coalition *et al.* Comments").

2 Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56, codified at 47 U.S.C. §§151 *et seq.* ("1996 Act").

3 As explained below, there is no evidence that UNE rates for unbundled local switching do not provide appropriate price signals to CLECs or fully compensate the ILEC. Although the Joint Commenters recognize that there are disputes as to how the Commission's TELRIC rules estimate the appropriate price for the loop (a dispute that is

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Commission adopted the *Triennial Review Order,*[4] it properly recognized that actual market conditions are relevant to an impairment analysis. The actual market evidence offers compelling evidence as to what works and what does not, and the BOCs comments cannot mask these basic facts.

A. UNE-L Inactivity Confirms Impairment In The Mass Market.

The focal point of BOCs' claims regarding local competition is the "UNE Fact Report" filed jointly by BellSouth, Qwest, SBC and Verizon.[5] Although labeled the UNE Fact Report, with respect to mass market competition, the analysis virtually ignores competition based on UNE-L. Rather, the Huber Report claims:

> The notion that voice service could be provided economically to mass market customers only by combining circuit switches with analog (narrowband) loops is now obsolete.[6]

Although the BOCs would prefer the Commission ignore the status of UNE-L based competition in the mass market, it remains the basic issue that the Commission must address to satisfy the D.C. Circuit. In the *Triennial Review Order*, the Commission unambiguously concluded that there is national impairment without access to the loop facilities

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exaggerated and without merit, but which nonetheless may exist), the ILECs never have put forth a coherent argument as to why local switching prices are not more than adequate at existing levels.

4 *See Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, Deployment of Wireline Services Offering Advanced Telecommunications Capability*, CC Docket Nos. 01-338, 96-98, 98-147, Report and Order and Order on Remand and Further Notice of Proposed Rulemaking, 18 FCC Rcd 16978 (2003), *corrected by Errata*, 18 FCC Rcd 19020 (2003), *reversed and remanded, United States Telecom Ass'n. v. FCC*, 359 F.3d 554 (D.C. Cir. 2004) ("*Triennial Review Order*").

5 UNE Fact Report, Peter Huber and Evan Leo (Kellogg, Huber, Hansen, Todd & Evans, P.L.L.C), WC Docket No. 04-313, CC Docket No. 01-38 (Oct.4, 2004) ("Huber Report").

6 Huber Report, II-1.

of the ILEC to offer analog voice services. This finding was not reversed in either *USTA I*[7] or *USTA II*.[8] The basic question as to whether voice service can be provided economically to mass market customers by combining CLEC-provided switches to analog loops is *exactly* the question that the Commission must answer for purposes of judging impairment for local switching.

There are two ways that entrants are able to access the loop to provide mass market POTS service: (1) installing their own switch and relying on manual hot cut processes, collocated facilities and transport backhaul to provide service, or (2) leasing local switching capacity from the ILEC, which is electronically connected to the monopoly loop plant. To determine whether the hot cut, collocation, and backhaul impairments impose a barrier to competition requires a comparison between UNE-L (loops *without* switching) and unbundled network element-platform ("UNE-P") (loops *with* switching) competitive activity. The difference in competitive activity measures the magnitude of impairment that frustrates one form of loop access from the other.

During the proceeding leading to the *Triennial Review Order*, the ILECs claimed that CLECs were routinely providing mass market services using their own switches. In this proceeding, however, the ILECs essentially ignore UNE-L competition, claiming that non-UNE based competition should be the standard of review. The reason can be found in the facts – the level of UNE-L competition in the mass market cannot justify a finding of non-impairment.

To begin, the Huber Report devotes only *three* paragraphs to UNE-L competition for mass market services via UNE-L. In those three paragraphs, the Huber Report admits that

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7 *United States Telecom Ass'n v. FCC*, 290 F.3d 415 (D.C. Cir. 2002) ("*USTA I*").

8 *United States Telecom Ass'n. v. FCC*, 359 F.3d 554 (D.C. Cir. 2004) ("*USTA II*").

the level of UNE-L competition was only 3 million lines at the time of the *Triennial Review Order* and has not changed.[9] This admission is relevant to two key conclusions. First, the admission confirms the evidence in the state *Triennial Review Order* proceedings that UNE-L based competition in the mass market is virtually non-existent, even nearly nine years after Congress passed the 1996 Act.[10] Inconsequential levels of competitive activity do not demonstrate non-impairment, particularly after so many years of entry and effort. Second, the measure most useful for calculating competitive *activity* is how conditions have changed over time. Even the ILECs admit that mass market UNE-L activity is "essentially the same as today,"[11] a phrase the ILECs apparently equate to declining activity that they choose not to emphasize.[12]

The important point is that a central fact is no longer in dispute – UNE-L penetration in the mass market is trivial and, when current activity is considered, is generally in decay. The ILECs no longer can claim that "actual marketplace activity" shows that carriers are unimpaired in their ability to access loop facilities without local switching, because even the facts as presented by the ILECs support the opposite conclusion.

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9 Huber Report, II-42 (stating, "[t]oday, the number of mass-market lines being served through unbundled loops and competitive circuit switches is approximately the same as it was at the time of the *Triennial Review* – roughly 3 million").

10 *See* PACE Coalition *et al.* Comments at 42.

11 *See Comments of Verizon*, WC Docket No. 04-313, CC Docket No. 01-338 at 14 (filed Oct. 4, 2004) ("Verizon Comments").

12 There is no question based on the data that the ILECs provided in the state *Triennial Review Order* proceedings that analog UNE-L volumes are declining. *See* PACE Coalition *et al.* Comments at 47.

B. TELRIC-Based Local Switching Rates Do Not Discourage UNE-L Competition.

Faced with the dilemma of contrary market evidence, the ILECs claim that it is the existence of unbundled local switching that discourages UNE-L competition.[13] For this claim to be plausible requires that local switching be systematically priced below the CLEC's incremental cost. As the Joint Commenters explain below, however, there is no theoretical or empirical support to such a claim – local switching UNE rates are, if anything, unreasonably *high*, particularly in comparison to the ILEC's "actual" central office switching expenses as reported in ARMIS.

First, it is important to emphasize what should be an obvious point – the relative attractiveness of UNE-L compared to UNE-P is completely independent of loop prices because the loop rate is essentially the same in either arrangement.[14] Consequently, whatever objection the ILECs have with the pricing of UNE Loops – and the Joint Commenters do not accept that UNE loops are priced incorrectly under TELRIC – that objection is irrelevant to whether UNE-P is correctly priced relative to UNE-L. Thus any claim that UNE-P is "priced too low" must focus exclusively on the pricing of local switching, because whatever economic incentive exists because loop pricing affects both strategies in the same way.[15]

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13 *See, e.g., Initial Comments of BellSouth Corporation*, WC Docket No. 04-313, CC Docket No. 01-338 at 19 (filed. Oct. 4, 2004) ("BellSouth Comments").

14 There are some minor rate differences in the BellSouth region, where the rate for the UNE-P combination is slightly lower than the sum of the rates of the individual loop and switch elements.

15 The Joint Commenters readily admit, however, that UNE-P enables carriers to purchase dramatically higher volumes of unbundled loops. That is precisely the point – unbundled local switching addresses impairments that otherwise prevent mass market competition using analog loops.

Second, it is important to understand that the Commission's TELRIC rules are fundamentally different for local switching than for other network elements. Whereas there is a continuing controversy as to whether "actual network conditions" are properly reflected in how the UNE loop rate is calculated, the ILEC's actual network topology of switching plays a large part in the existing TELRIC rules because the number of wire centers (and, therefore, the number and location of switches) is fixed in the TELRIC model.

This assumption effectively imposes on CLECs that lease unbundled local switching the cost consequences of the ILEC's inefficient network architecture (relative to today's technology) that relies on far too many wire centers, and therefore local switches, than would be needed if the ILEC re-optimized its network based on forward-looking technology. The fact that the ILEC networks inefficiently concentrate loop facilities by having too many wire centers imposes a serious impairment on CLEC networks that can only be (partially) offset by the CLEC leasing switching directly from the ILEC.[16] For those CLECs that lease switching, however, this inefficiency is also built into the TELRIC price because the Commission rules preclude states from re-optimizing ILEC networks to reflect fewer, and thus more efficient, ILEC switches. This view – that the TELRIC rules do not impact how switching costs are calculated – is shared by one ILEC, BellSouth:

> It is important to note that even though the fundamental cost methodologies (i.e., TSLRIC and TELRIC methodologies are similar ... it is the additional constraints currently mandated by the FCC that the incumbent local exchange carriers (ILECs) object to

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16 *See* Letter from the PACE Coalition, *et al.*, to Ms. Marlene Dortch, Secretary, Federal Communications Commission, CC Docket Nos. 01-338, 96-98, 98-147 (Dec. 11, 2002), attached hereto as Exhibit 1. The analysis in this letter documents that legacy ILEC networks are characterized by many wire centers serving few loops, thereby increasing CLEC collocation and transport costs.

> with respect to TELRIC-based rates. The use of a hypothetical network and most efficient, least-cost provider requirements have distorted the TELRIC results and normally understate the true forward-looking costs of the ILEC.
>
> These distortions, however, are most evident in the calculation of unbundled loop elements, and they are less evident in the switching and transport network elements ....
>
> ***
>
> ...I emphasize that the main cost drivers for end office switching are the fundamental unit investments, which are identical in switching TSLRIC and TELRIC studies.[17]

Third, as with all of the Commission's TELRIC rules, the end result of the methodology is a price based on the average *total* cost of the element in question, albeit an average total cost based on new technology. In the case of local switching, where states have not based rates on new packet-technologies, and where ILEC average switching costs are inflated because the average utilization of its switches is reduced by having too many switches serving too few loops, the methodology assures that the average-cost TELRIC rate far exceeds the incremental cost of any CLEC facility. Consequently, it is economically impossible for the pricing of unbundled local switching to discourage a CLEC from using its own switch – unless, of course, there are substantial impairments/barriers that prevent the CLEC switch from being able to access to loop. As the ILECs routinely claim, there is substantial CLEC switching capacity, much of it installed despite the availability of unbundled local switching,[18] which both proves that the availability of local switching has not discouraged CLECs from deploying

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17 Direct Testimony on Robert McKnight on behalf of BellSouth, Public Service Commission of South Carolina ("McKnight Direct"), Docket No. 1997-239-C, (filed Dec. 31, 2003) at 7, 9, attached hereto as Exhibit 2.

18 The Huber Report claims that there are 1,200 CLEC circuit switches, roughly 500 more than existed in 1999. (I-2).

switches and that economic barriers to use the excess capacity on these switches to provide mass market services are preclusive and widespread.

Finally, there is no evidence that *implies*, much less demonstrates, that the ILEC is not being adequately compensated under the UNE local switching rates established by the states. Table A (below) compares the average UNE price for local switching to the average "Central Office Switching Expense" that each BOC has reported.[19] As shown in Table A, the rates CLECs paid to lease local switching are 3 to 7 times more than the average Central Office Switching Expense incurred by the BOCs, clearly contributing to the BOCs' common and capital costs.[20]

Table A: Comparing Average Switching Expense to UNE Switching Rate ($/line/month)

BOC	Central Office Switching Expense	Average UNE Switching Rate[21]	Ratio of UNE Rate to Expense
BellSouth	$1.30	$5.68	4.4
Qwest	$1.11	$4.53	4.1
SBC	$1.39	$4.53	3.2
Verizon	$0.72	$4.98	6.9
Average	$1.13	$4.89	4.3

To place the contribution received from unbundled local switching in context,[22] the Joint Commenters have calculated the comparable overall ratio of revenues-to-expenses (less

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19 ARMIS 43-03, Row 6210, Central Office Switching Expense.

20 It is not possible to separately extract from ARMIS an estimate of that portion of depreciation expense related to central office local switching.

21 *See* Updated UNE Rates, REGULATORY SOURCE ASSOCIATES (Aug. 16, 2004). Average UNE rate calculated assuming average DEM minutes and BOC averages weighted applying the UNE-P volumes per state reported to the Commission as of December 2003. For those states with deaveraged local switching rates, the rate in the lowest priced zone is used.

22 The term "contribution" is used here to refer to the ratio of revenue-to-expense received from unbundled local switching, with ratios above one contributing to the BOC's

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depreciation)[23] for each BOC. As Table B shows, the revenue-to-expense contribution achieved by the existing UNE local switching prices is dramatically higher than the contributions any of the BOCs receive from its services overall, frequently by a factor of two or more.

Table B: Comparing Switching Contribution to Contribution Overall

BOC	Ratio of UNE Local Switching Rate to Switching Expense	Overall Ratio of Revenue to Expense
BellSouth	4.4	2.1
Qwest	4.1	2.0
SBC	3.2	1.8
Verizon	6.9	1.6
Average	4.3	1.8

Finally, the Joint Commenters have computed the effect of the proposed $1.00 per month increase in local switching rates suggested in the *Interim Rules Order*.[24] As shown in Table C, this arbitrary increase in local switching rates – an increase that ultimately will be paid by the American consumer and small business – increases the average local switching price by 20%, nearly compensating the BOC for its central office expenses by an additional factor (that is, by compensating the BOC for *five* times its average expense, instead of the *four* times achieved by the cost-based rates).

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common costs, as well as the capital costs of local switching (depreciation and return) that cannot be specifically identified through ARMIS.

23 As noted, ARMIS does not permit us to specifically identify the depreciation attributable solely to central office switching. Because this value cannot be determined for switching, the Joint Commenters have excluded it from the company-wide calculation to assure comparability.

24 *Unbundled Access to Network Elements*, WC Docket No. 04-313; *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, CC Docket No. 01-338, Order, FCC 04-179 at ¶ 29 (rel. Aug. 20, 2004) ("*Interim Rules Order*").

Table C: Effect of FCC's Proposed Rate Increase on Local Switching

BOC	Existing Local Switching Rate /Line	Proposed Local Switching Rate/Line	Percent Increase	Revenue-to-Expense Ratio (Proposed Rates)
BellSouth	$5.68	$6.68	18%	5.1
Qwest	$4.53	$5.53	22%	5.0
SBC	$4.53	$5.53	22%	4.0
Verizon	$4.98	$5.98	20%	8.3
Average	$4.89	$5.89	20%	5.2

As the above tables indicate, there is no evidence to suggest that rates for unbundled local switching inadequately compensate the BOCs or provide price signals to new entrants that discourage facilities investment. To the contrary, if anything, the above analysis demonstrates that the existing rates are at the upper end (or beyond) of the just and reasonable range. The fact that CLECs would incur such local switching costs is evidence that barriers to loop access can be surmounted only through the lease of local switching, even where such lease rates are systematically high (as are the rates for UNE switching under the fixed-wire center, TELRIC rules).

C. The So-Called Intermodal Alternatives Comprise Distinct Markets And Do Not Challenge Impairment.

As explained in the Joint Commenters' initial comments and reiterated briefly below, the so-called intermodal alternatives highlighted by the BOCs do not override the impairment analysis for the POTS market. Intermodal alternatives prove nothing concerning impairment, which is fundamentally tied to the incumbent's loop network. Such alternatives would be sufficient only if they rendered loop access irrelevant – a circumstance they are far from achieving.

The Joint Commenters already have explained at length why intermodal alternatives are not substitutes for POTS service and will not repeat that analysis here.[25] There are substantial differences between wireless, cable and, most dramatically, VoIP services, that cause each to define a separate market.[26] Wireless services represent a mobile complement to wireline service, while VoIP services require broadband access connections that exclude such customers from properly being considered part of the analog mass market.

Although the ILECs' comments maintain that intermodal alternatives are sufficient, what little data they provide does not support the claim. For instance, the claim that more customers are moving from wireline-to-wireless service is the product of a comparison between one unsupported estimate (3-5%)[27] with another (7-8%) attributed to an author who offers "it is admittedly difficult" to get an accurate handle on how much substitution is actually occurring.[28] Moreover, as the Huber Report admits, estimates of wireless substitution are influenced by a focus on "the population that are single between the ages of 20 and 34 [and] are most likely to disconnect their wireline phone for a wireless phone."[29] Basing regulatory

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25 *See* PACE Coalition, *et al.* Comments, at 11.

26 Among the intermodal alternatives, "traditional" cable telephony (based on circuit switched architecture) is closest to wireline POTS service. However, the strategy was never broadly adopted by the cable industry which appears, at this time, to be focusing on VoIP applications that combine voice and data services.

27 The oft-cited 3-5% figure is the result of a Yankee Group estimate and claim by the CTIA. *See* Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993, Annual Report and Analysis of Competitive Market Conditions with Respect to Commercial Mobile Services, Sixth Report, 16 FCC Rcd 13350, fn. 207 (2001).

28 *The Current State of Competition in the Communications Marketplace Before the House Subcommittee on Telecomms. & the Internet, Committee on Energy & Commerce*, 108th Cong. (Feb. 4, 2004) (testimony of Michael J. Balhoff, Legg Mason, Inc.), attached hereto as Exhibit 3.

29 Huber Report, II-29.

decisions on the unique purchasing patterns of this demographic would not represent sound public policy.

With respect to VoIP service, the Huber Report is largely a collection of analyst projections as to how VoIP *may* grow in the next three to seven years. With respect to *actual* market experience, the report cites to less than 500,000 lines,[30] and the highest *estimate* of current penetration levels is only one million lines at the end of 2004.[31] Moreover, a UBS report estimates that total cable telephony lines – including VoIP – will only reach 11 million lines by the end of the decade,[32] an estimate that is consistent with the projections cited in the Huber Report.[33] In contrast, there are 17 million lines using unbundled local switching today – 60% more than VoIP is expected to reach by 2010.

The Joint Commenters do not dismiss the idea that VoIP may be a factor in the future, and may indeed, over time, grow to define a market that is larger than traditional POTS. The facts, however, are that (1) there are substantial differences between VoIP products and POTS today, and (2) the levels of VoIP penetration to date reinforce the view that consumers themselves do not see the services as substitutes. Moreover, even if all customers with high-speed data connections ultimately did consider VoIP the equal of traditional POTS, the millions of customers *without* broadband access would still define a separate POTS-only market in which

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30 Reported actual VoIP levels in the Huber Report are for Cablevision (115,000 – Huber Report, II-5), Time-Warner in Raleigh (20,000 – Huber Report, II-8) and Portland (12,000 – combining Huber Report II-5 and *Cable World* May 26, 2003), and Vonage (275,000 – UNE Fact Report II-11).

31 Table 3, Huber Report II-9.

32 *Gallup Survey Highlights VoIP Potential*, UBS INVESTMENT RESEARCH at 8, (Apr. 8, 2004), attached hereto as Exhibit 4.

33 Huber Report, Table 3 (II-9) (offering estimated penetration by 2006 of between 7.7 and 11.7 million lines).

the Commission would need to evaluate the impairments associated with offering analog voice services.

Finally, the Joint Commenters note that any attempt to "weight" non-wireline alternatives to adjust for the fact that such intermodal services are not substitutes would be arbitrary, as exemplified by the scheme proposed by the New York State Department of Public Service ("DPS").[34] In its comments, the New York DPS proposes a scheme of "impairment weights" in which it assigns a value to various competitive conditions. The little information the New York DPS has provided on how its scheme would be applied in New York, however, demonstrates that its proposal is fundamentally arbitrary and capricious.[35]

First, the New York DPS never explains how *any* of its proposed weights usefully measure the impairments confronting a carrier seeking to offer mass market voice services to analog customers. For example, the fact that a cable company is offering cable modem service to customers in a wire center has nothing to do with any of the impairments that frustrate POTS competition. The cable company does not experience a hot cut, it does not collocate equipment, it does not backhaul traffic – in fact, under the New York DPS system, it does not even have to offer voice service and yet it "counts" for purposes of determining impairment.

Second, the New York DPS offers no explanation as to how any of the relative weights make sense, even if one ignores that they are unrelated to impairment. For instance,

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34 *See Comments of the New York Department of Public Service*, WC Docket No. 04-313, CC Docket No. 01-338 at iii – iv (filed Oct. 4, 2004) ("New York DPS Comments").

35 Specifically, under the New York DPS "methodology" different competitors are assigned a specific "impairment value." For instance, two wireless carriers would be assigned a value of 0.5, while a cable modem provider would be assigned a value of 0.75. The various values are summed, and in wire centers with an impairment index of 2.75, carriers would not be able to lease unbundled local switching.

under the New York DPS scheme, the competitive significance of two wireless carriers is assumed to be equal to one UNE-L provider that does not offer mass market service (*i.e.*, each is assigned an intermodal weight of 0.5), but either is 1/3 less meaningful than a carrier offering DSL or cable modem service (which is worth a value of 0.75).

Finally, the New York DPS never explains how the aggregate value of 2.75 suggests that a new entrant is not impaired, or even that there is sufficient competition to a wire center for the impairment analysis to be ignored. The New York DPS's application of its methodology in New York demonstrates just how arbitrary and capricious – indeed absurd – is the methodology. The premise of the methodology is that the weights somehow meaningfully track competitive conditions; yet, if that were true, there would be *some* observable relationship between index values and the competition faced by UNE-P carriers in each wire center.[36] As shown in Table D no such relationship can be found.

Table D: Comparing the New York DPS Impairment Index with Known Competitive Conditions

"Impairment" Index	UNE-P Penetration in Wire Centers with Same Index Value
0.5	16.6%
1.25	16.8%
1.75	19.3%
2.25	17.1%
2.75	20.8%
3.25	15.7%

As shown above, the New York DPS "impairment index" bears no rational relationship to competitive conditions. In fact, a statistical analysis suggests an entirely random

[36] The only competitive information that the New York DPS provides to measure the level of competition in wire centers with equal index values is UNE-P penetration. *See* New York DPS Comments at iv.

relationship.[37] Such a conclusion should be expected, however, since the "methodology" is completely divorced from any measure of the factors that produce impairment in the POTS market, it offers no rational linkage between its proposed weights and actual competitive conditions, and provides no basis for its recommendation that an index value of 2.75 should equate to a finding of non-impairment. In other words, the only way that the methodology could have resulted in an observed relationship between its index values and competition is through random effect (and it failed even at that).

III. STATE COMMISSIONS HAVE THE AUTHORITY TO ADOPT UNBUNDLING OBLIGATIONS

The Commission must reject the BOCs' attempts to remove authority from the states to promote local competition through the adoption of unbundling requirements. Essentially, the BOCs have sought to divest the states of any authority that they have under the Act and their own state statutes to regulate network elements, to approve negotiated agreements, or to take any other action to further the goal of a competitive market for basic voice telephone services.

There is no merit to the BOCs' arguments that the states only have a consultative role in the section 271 process, and that a state's role ends when it makes a recommendation to the Commission regarding the BOC's application for in-region interLATA authority under section 271 of the Act. To the contrary, under the plain language of the Act and their own state statutes, state commissions have authority that extends beyond a consultative role. It would be

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37 The number of observations and data provided by the New York DPS does not permit meaningful statistical analysis. Even a simple correlation analysis suggests the methodology produces random results.

unlawful for the Commission to adopt – as the BOCs have suggested – a blanket rule prohibiting the states from exercising any regulation of network elements beyond that boundary.

A. The States Have Authority Under The Act And Their Own State Statutes To Promote Competition Through Market Opening Rules.

State commissions have authority under the 1996 Act and their own state statutes to adopt unbundling rules and other requirements that foster competitive entry in local telecommunications markets. In the 1996 Act, Congress has set forth a dual role for the Commission and the states. In section 251(d)(3), Congress explicitly preserves the states' regulatory authority:

> (3) PRESERVATION OF STATE ACCESS REGULATIONS. – In prescribing and enforcing regulations to implement the requirements of this section, the Commission shall not preclude the enforcement of any regulation, order, or policy of a State commission that –
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> (A) establishes access and interconnection obligations of local exchange carriers;
>
> (B) is consistent with the requirements of this section; and
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> (C) does not substantially prevent implementation of the requirements of this section and the purposes of this part.

Section 251(d)(3) specifically prohibits the Commission from taking any action that impedes a state's ability to "establish[] access and interconnection obligations of local exchange carriers so long as such obligations do not conflict with the Act's goal of promoting competition in the basic telephone services market."[38] Requiring ILECs to unbundle their local exchange networks and afford CLECs "access and interconnection" to their network elements clearly fall within the

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38 47 U.S.C. § 251(d)(3).

scope of authority designated to the states in section 251(d)(3)(A) and is consistent with the requirements of subsections (B) and (C).[39]

In reviewing the Commission's interpretation of section 251(d)(3), the United States Court of Appeals for the Eighth Circuit held:

> It is entirely possible for a state interconnection or access regulation, order, or policy to vary from a specific FCC regulation and yet be consistent with the overarching terms of section 251 and not substantially prevent the implementation of section 251 or Part II. In this circumstance, subsection 251(d)(3) would prevent the FCC from preempting such a state rule, even though it differed from an FCC regulation.[40]

Significantly, section 251(d)(3) measures the lawfulness of state regulation by its consistency with the Act and its purposes, not by its consistency with the Commission's policy preferences.

In addition, states have authority to require unbundling under their own state statutes.[41] The right of the states to exercise their independent unbundling authority has been confirmed by the Eighth Circuit:

> . . . subsection 252(c)(1) does require state commissions to ensure that arbitrated agreements comply with the Commission's regulations made pursuant to section 251, but by its very terms this provision confines the states only when they are fulfilling their roles as arbitrators of agreements pursuant to the federal Telecommunications Act of 1996. This provision does not apply to state statutes or regulations that are independent from the

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39 The BOCs cannot legitimately argue that a state commission determination that unbundling is necessary to further competition would be in conflict with the Act's "purpose" (*i.e.*, to create a fully competitive telecommunications arena throughout the United States).

40 *Iowa Utils. Bd. et al. v. FCC,* 120 F.3d 753, 806 (8th Cir. 1997) Notably, this aspect of the Eighth Circuit's decision was not appealed to the Supreme Court.

41 *See, e.g., Staff of the Illinois Commerce Commission's Initial Comments, Illinois Bell Telephone Company, Filing to Implement Tariff Provisions Related to Section 13-801 of the Public Utilities Act*, ICC Docket No. 01-0614 (filed Oct. 4, 2004) (discussing Illinois's unbundling statute), attached hereto as Exhibit 5.

> Telecommunications Act of 1996. *Many states enacted legislation designed to open up local telephone markets to competition prior to the 1996 federal Act . . . and subsection 251(d)(3) was designed to preserve such work of the states.*[42]

The Joint Commenters support the comments of the state public utility commissions, including, for example, Pennsylvania, which have argued that the Commission must not preclude the states from exercising their own authority.[43] As these commissions have explained, state commissions are in the best position to evaluate the particular competitive conditions in their states and determine how best to promote the public interest through exercise of their statutory authority.[44]

B. The Commission Already Has Concluded That A State Commission's Section 271 Authority Extends Beyond A Consultative Role.

Nothing in the 1996 Act or in the Commission's rules and orders limits a state's role solely to providing a recommendation about whether a BOC is eligible to obtain in-region interLATA authority under section 271 of the Act, as the BOCs have argued.[45] Indeed, the Commission already has acknowledged that state regulators share responsibility with the Commission for ensuring compliance with section 271 of the Act and that a state's role under section 271 does not end when the state makes a recommendation to the Commission regarding the BOC's application to provide in-region interLATA service in that state. In particular, the

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42 *See Iowa Utils. Bd.*, 120 F.3d at 807 *(emphasis supplied).*

43 *See, e.g., Comments of the Pennsylvania Public Utility Commission*, WC Docket No. 04-131, CC Docket No. 01-338 at 3 (filed Oct. 4, 2004) (stating that "states have authority under section 251(d)(3) to establish unbundling obligations to address local circumstances...") ("Pennsylvania PUC Comments").

44 *See, e.g.,* Pennsylvania PUC Comments at 3 (stating "the national policy should favor the ability of state commissions to consider the various local circumstances in determining their unbundling obligations.").

45 *See, e.g.,* Verizon Comments at 122.

Commission specifically endorsed a state's continued enforcement role by inviting carriers to bring post-entry complaints to the state commission in the first instance:

> Complaints involving a BOC's alleged noncompliance with specific commitments the BOC may have made to a state commission, or specific performance monitoring and enforcement mechanisms imposed by a state commission, should be directed to that state commission rather than the FCC.[46]

In adopting Verizon's application to provide long distance services in New York, the Commission emphasized that it intended to work "in concert" with state commissions after the carrier had obtained section 271 approval.[47] The Commission made similar pronouncements when it approved subsequent BOC applications for in-region interLATA authority, thus confirming that a state's role does not end when it submits a recommendation to the Commission regarding the BOC's application for in-region interLATA authority under section 271 of the Act.[48] Accordingly, the Commission again should reject the BOCs' claim that the states are prohibited from taking any action under section 271 beyond recommending that a BOC obtain interLATA operating authority.[49]

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46 *Application by Bell Atlantic New York for Authorization Under Section 271 of the Communications Act to Provide In-Region, InterLATA Service in the State of New York*, 15 FCC Rcd 3953 ¶ 452 (1999) ("*New York 271 Order*").

47 *See New York 271 Order* ¶ 452 (stating, "[w]orking in concert with the New York Commission, we intend to monitor closely Bell Atlantic's post-entry compliance...").

48 *See, e.g., Joint Application by SBC Communications Inc., Southwestern Bell Tel. Co., and Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance for the Provision of In-Region, InterLATA Services in Kansas and Oklahoma*, 16 FCC Rcd 6237 ¶ 10 (2001) (stating, "we are confident that cooperative state and federal oversight and enforcement can address any backsliding that may arise with respect to SWBT's entry into the Kansas and Oklahoma markets.").

49 *See, e.g., Comments of Qwest Communications International, Inc.*, WC Docket No. 04-313, CC Docket No. 01-338 at 94 (filed Oct. 4, 2004) ("Qwest Comments"). *See also* Verizon Comments at 121 (arguing that the "only role Congress identified for state commissions is derivative of a task Congress assigned to the Commission"); BellSouth Comments at 79.

C. The Commission Cannot Adopt A Blanket Rule Preempting State Action.

The Commission must reject SBC's and Verizon's requests that the Commission adopt a blanket rule prohibiting any potential action that a state might take to require unbundling.[50] The BOCs are asking the Commission to preempt state commission action before any state has acted and before it can be determined whether the state action actually conflicts with a Commission determination on the merits of the issue. As the court in *USTA II* acknowledged, claims that state actions that have not yet occurred should be preempted are not ripe.[51]

Preemption is not a tool to be used lightly; the Supreme Court has cautioned that courts should "start with the assumption that the historic powers of the states [are] not to be superceded by [a] federal act unless that was the clear and manifest purpose of Congress."[52] In this situation, courts have held that the Act "contains a general anti-preemption clause."[53] Thus, preemption of state law only is justified if it is determined that a particular state law at issue actually is in direct conflict with the Act or the Commission's rules that were promulgated in furtherance of the Act.[54] Preemptive preemption is never justified. Furthermore, adopting a blanket prohibition is overbroad; it is not until the Commission evaluates a particular regulation

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50 *See Comments of SBC Communications Inc.*, WC Docket No. 04-313, CC Docket No. 01-338 at 115 (filed Oct. 4, 2004) ("SBC Comments"); Verizon Comments at 120-25.

51 *USTA II*, 359 F.3d at 594.

52 *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947).

53 *AT&T Communications of Ill. v. Illinois Bell Tel. Co.*, 349 F.3d 402, 410 (7th Cir. 2003) (quoting 47 U.S.C. § 601(c), 110 Stat. 56 (1996) (note to 47 U.S.C. § 152 ("This Act and the amendments made by this Act shall not be construed to modify, impair, or supercede Federal, State, or local law unless expressly so provided in such Act or amendments."))

54 *Indiana Bell Tele. Co. v. McCarty*, 362 F.3d 378, 392 (7th Cir. 2004) (citing and quoting 47 U.S.C. § 261(c)).

and the state's exercise of authority that a determination can be made as to whether that particular regulation is in conflict with federal policy.

In *USTA II*, the state petitioners claimed that the *Triennial Review Order* "improperly preempts state unbundling regulations that exist independent of the Commission's federal unbundling regulations enacted pursuant to [section] 251."[55] In the *Triennial Review Order*, the Commission had required "[p]arties that believe that a particular state unbundling obligation is inconsistent with the limits of section 251(d)(3)(B) and (C)" to seek a declaratory ruling from the Commission.[56] The court concluded that the states' challenge was unripe, and that the state petitioners would not encounter harm by deferring "judicial review of the preemption issues until the FCC actually issues a ruling that a specific state unbundling requirement is preempted."[57]

The same rationale applies to the BOCs' requests. In other words, it would be unlawful for the Commission to issue a blanket rule – as the BOCs have requested – that preempts any and all potential state unbundling actions. Whether preemption of a specific state unbundling rule is justified is a fact-specific inquiry that the Commission must decide on a case-by-case basis. Accordingly, the Commission must deny the BOCs' request to preempt any and all state unbundling actions, including those actions that states have not yet taken.

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55 *USTA II*, 359 F.3d at 594.

56 *Triennial Review Order* ¶ 195.

57 *USTA II*, 359 F.3d at 594.

IV. CARRIERS MUST COMPLY WITH THE CHANGE OF LAW PROVISIONS IN THEIR AGREEMENTS TO IMPLEMENT THE UNBUNDLING RULES ADOPTED BY THIS COMMISSION

The Commission must reject Verizon's blatant attempt to unilaterally change the provisions in its interconnection agreements with CLECs without following the change of law processes specified in those agreements.[58] There is no merit to Verizon's argument that a Commission finding of no impairment does not constitute a change of law.[59] Verizon's argument is preposterous. As stated in the Joint Commenters' initial comments, the court's decision in *USTA II* does not mandate a finding of no impairment with regard to any particular network element, in general, and local switching, in particular.[60] As such, if the Commission were to conclude in this proceeding that carriers are not impaired without unbundled access to a particular network element, then the Commission would not – as Verizon contends – be implementing any particular directive of federal law. The entire premise upon which Verizon's argument is based – that federal law *requires* a Commission decision eliminating unbundling – is flawed.

There is no doubt that any rules that the Commission adopts in this proceeding will constitute a change of law under the vast majority of interconnection agreements in place today. When the parties negotiated and arbitrated their current agreements, they did so with an understanding of the law in effect at that time, pursuant to which ILECs were required to provide

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58 Verizon Comments at 132-33.

59 *Id.* at 133 (arguing "when the Commission, conducting an impairment analysis pursuant to *USTA II* and other binding guidance from the Supreme Court and the D.C. Circuit, does not find impairment, it has not changed the law; it has merely followed federal law, as it always has existed.").

60 *See* PACE Coalition, *et al.* Comments at 38-40.

certain unbundled network elements to requesting carriers. Any change in unbundling obligations that results from this proceeding constitute a change of law. Accordingly, carriers must follow the change of law provisions in their agreements to implement the rules adopted in this proceeding.

Even if the Commission adopts new unbundling rules that are effective immediately, carriers still must comply with the change of law requirements in their agreements to effectuate those rules. The Commission must reject USTA's and Verizon's request that the Commission abrogate interconnection agreements by mandating that any unbundling rules take effect immediately regardless of the change of law provisions in carriers interconnection agreements.[61] Verizon suggests that the Commission can unilaterally change the terms of carriers' interconnection agreements on the ground that, in Verizon's opinion, the Commission's new rules would affect interconnection agreements in an identical manner.[62] Carriers have entered into myriad interconnection agreements that vary significantly in scope and substance, and it is unrealistic, not to mention patently incorrect, to assume that any particular rule that the Commission adopts will affect all interconnection agreements or even a subset of interconnection agreements in an identical manner. As such, the Commission must reject Verizon's arguments, and confirm that carriers must follow the change of law provisions in their interconnection agreements. Indeed, other BOCs, such as Qwest, acknowledge that ILECs must abide by the

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61 *See, e.g., Comments of the United States Telecom Association*, WC Docket No. 04-313, CC Docket No. 01-338 at 26 (filed Oct. 4, 2004) (requesting that the FCC "affirmatively state that its new rules are effective immediately") ("USTA Comments"); Verizon Comments at 132-33.

62 *See* Verizon Comments at 133.

change of law provisions in their agreements to effectuate any rules that the Commission adopts in this proceeding.[63]

Verizon would have the Commission believe that interconnection agreements only pertain to network elements provided under section 251(c)(3) of the Act. In reality, interconnection agreements frequently contain numerous provisions other than those implementing the ILEC's obligations under section 251(c)(3), including provisions pertaining to obligations under other subsections of section 251, section 271, and state law. As such, even if the Commission modifies an ILEC's obligations under section 251(c)(3), other provisions of the carriers' agreements would remain unaffected. In addition, even if interconnection agreements only pertained to section 251(c)(3) network elements, which they do not, the Commission still cannot lawfully interfere with the parties' contractual obligations under those agreements. The Commission cannot endorse Verizon's attempt to eviscerate numerous interconnection agreements that it has entered into with CLECs.

In rejecting Verizon's arguments that change of law provisions do not apply, the Commission also must reject SBC's request that the Commission find that it is presumptively bad faith if carriers do not amend their interconnection agreements within thirty (30) days of the Commission's new rules. First, most interconnection agreements contain provisions specifying timeframes for amending those agreements if a change in law occurs. The Commission cannot lawfully supercede those contractual provisions. Second, contrary to SBC's arguments, these

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63 *See* Qwest Comments at 92 (stating that "ILECs should be permitted to discontinue provision of such network elements as UNEs to existing customers in accordance with the change-of-law provisions in their interconnection agreements...").

amendments are not "exceedingly simple."[64] Carriers generally are parties to numerous interconnection agreements (and frequently with different ILECs), and they need time to draft, evaluate, and revise proposed amendments to those contracts. As the Joint Commenters stated in their initial comments, it will take time and money for CLECs to transition to non-UNEs.[65] CLECs also need to evaluate whether they can continue to serve all of the markets in which they currently operate and where to focus their resources. Accordingly, SBC's proposal is simply unworkable and must be rejected.

V. THE IMPAIRMENT STANDARD IN THE *TRIENNIAL REVIEW ORDER* IS CONSISTENT WITH THE COURT'S REASONING IN *USTA II*

In the *Triennial Review Order*, the Commission established a standard for determining when, applying section 251(d)(2), a CLEC would be "impaired" by a denial of access to a non-proprietary network element. The Commission defined impairment as "an entry barrier or barriers to entry, including operational and economic barriers, that are likely to make entry into a market uneconomic."[66] The Commission focused its impairment analysis on five types of entry barriers that CLECs face as a result of the ILEC's natural monopoly in the POTS market, including barriers resulting from: (1) economies of scale, (2) the existence of sunk costs, (3) "first-mover" advantages, (4) absolute cost advantages, and (5) barriers within the control of the ILECs.[67] The court in *USTA II* specifically refrained from any general criticism of the Commission's general impairment standard articulated in the *Triennial Review Order*, finding that the Commission "explicitly and plausibly" connected the factors to be considered in the

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64 SBC Comments at 22.

65 *See* PACE Coalition *et al.* Comments at 91-96.

66 *Triennial Review Order* ¶ 84.

67 *Id.* ¶¶ 87-91.

analysis to natural monopoly characteristics and or to other structural impediments to competitive supply, such as sunk costs, ILEC absolute cost advantages, first-mover advantages, and operational barriers to entry within the control of the ILEC.[68] This analytic framework should be retained, because nothing in the *USTA II* decision brings it into question. The Commission applied this impairment standard to correctly reach a national finding of impairment based on the evidence provided in the *Triennial Review Order* proceeding. The evidence obtained in state commission impairment dockets and provided in the comments submitted this docket further supports a national finding of impairment.

A. There Is No Reason To Reformulate The Impairment Standard Adopted In The *Triennial Review Order.*

The impairment standard to be applied in this proceeding should continue to be "[a] lack of access to an incumbent LEC network element [which] poses a barrier to entry, including operational or economic barriers, that are likely to make entry into a market uneconomic."[69] In the *Triennial Review Order,* the Commission adopted the correct approach informed by the consideration of relevant entry barriers and the examination of other evidence that entry into the relevant market is uneconomic, especially evidence whether entry into the market has already occurred in both geographic and customer markets without reliance on the ILEC's network, *i.e.,* through self-provisioning or reliance of third-party provisioning.[70] The Commission's approach rightfully took into account "customer class, geography, and service,"[71]

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68 *USTA II*, 359 F.3d at 572.

69 *Triennial Review Order* ¶ 84.

70 *Id.*

71 *Id.* ¶ 118.

finding that distinct market segments existed for mass market and enterprise customers.[72] In addition, the types of services that CLECs might offer using the network elements in competition with traditional ILEC POTS services were also considered.[73] The Commission correctly identified the necessary avenues of inquiry into an impairment analysis, and based its findings on these enumerated factors. None of the aspects of the Commission's *Triennial Review Order* impairment standard require change. The Commission should not now abandon this approach.

1. *The Commission may use the "at a minimum" language in section 251(d)(2) to make unbundling determinations in the absence of impairment.*

Notwithstanding the claims of Qwest,[74] the "at a minimum" language of section 251(d)(2) affords the Commission the flexibility to look beyond impairment to determine whether a given network element must be made available as a section 251(c)(3) network element. In reviewing the Commission's use of the phrase "at a minimum" in the *UNE Remand Order*,[75] the court in *USTA I* found no fault in the Commission's determination that the express language of section 251(d) permitted the Commission to consider factors outside those enumerated in section 251(d)(2)(A) and (B) when making unbundling determinations.[76] The

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72 *Id.* ¶ 123.

73 *Id.* ¶ 141.

74 *See* Qwest Comments at 13.

75 *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-98, Third Report and Order and Fourth Further Notice of Proposed Rulemaking, 15 FCC Rcd 3696 (1999) ("*UNE Remand Order*"), *petitions for review granted, United States Telecom Ass'n. v. FCC,* 290 F.3d 415 (D.C. Cir. 2002), *cert. denied,* 538 U.S. 940 (2003).

76 *USTA I*, 290 F.3d at 425.

USTA I court merely cautioned the Commission against ordering the "widest unbundling possible" without connecting unbundling requirements to "something a bit more concrete."[77]

In response to the *USTA I* decision, the Commission applied the phrase "at a minimum" in section 251(d)(2) with restraint, determining that while the statute gave the Commission authority to determine "other" factors for justifying unbundling, the record did not indicate "any other factors that would require unbundling in the absence of impairment."[78] As such, the Commission determined it would "continue to weigh other factors that may be relevant to a particular unbundling determination, but we will do so with an eye to the specific goals of the Act, as the DC Circuit has indicated we may do."[79] The Commission further determined that the phrase "at a minimum" did not limit its determinations to those that restrict the ILECs' unbundling obligations nor did it permit the Commission to require unbundling only if all the goals of the 1996 Act are satisfied.[80] The court in *USTA II* reaffirmed the Commission's right to "examine the full context" and to order unbundling in situations where impairment does not exist.[81] As such, the Commission's current interpretation of "at a minimum" was appropriately applied in the *Triennial Review Order* and should continue to be applied in the same manner in this proceeding.

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77 *Id.*

78 *Triennial Review Order* ¶ 173.

79 *Id.*

80 *Id.* ¶ 174.

81 *USTA II*, 359 F.3d at 572.

2. *Commission met its burden by making a national finding of impairment.*

The Commission met its burden when it established a national finding of impairment for mass market local switching.[82] In the *Triennial Review Order*, contrary to claims by Verizon, the Commission did not impose a nationwide unbundling obligation on the ILECs for mass market local switching because it could not determine exactly where competitors are not impaired rather than determining where impairment existed.[83] To the contrary, the Commission based its impairment finding in the *Triennial Review Order* on the substantial record evidence submitted by both ILECs and CLECs that economic and operational impairment existed on a national basis for mass market switching. Specifically, the Commission determined that CLECs face economic and operational barriers caused by the ILECs' hot cut process, including "the associated non-recurring costs, the potential for disruption of service to the customer and . . . that incumbent LECs appear unable to handle the necessary volume of migrations to support competitive switching in the absence of bundled switching."[84] And, as discussed by the Joint Commenters in their initial comments, the rightness of this conclusion has been shown by the data complied in the state impairment dockets.

Verizon makes the empty claim that CLECs have withheld relevant information that proves non-impairment.[85] Verizon provides no support for this accusation, nor does any exist. The *Triennial Review Order* record was replete with evidence of the impairments faced by CLECs seeking to serve mass market customers and this evidence has now been confirmed in the

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82 *Triennial Review Order* ¶ 419.

83 *See* Verizon Comments at 8 (emphasis omitted).

84 *Triennial Review Order* ¶ 459.

85 Verizon Comments at 9-10.

post *Triennial Review Order* records developed in the states. For example, in an extensive report summarizing the evidential record established in the *Triennial Review Order* proceeding of the California Public Utilities Commission ("California PUC"), the California PUC Staff concluded that "there are no markets (defined by wire centers) that contain at least three CLECs with self-deployed switches providing UNE-L mass market service."[86] Summaries of other state *Triennial Review Order* proceedings provided as comments in this docket also confirm the Commission's national finding of impairment for mass market switching.[87] In New Jersey, for example, summary of the testimony submitted in the New Jersey Board of Pubic Utilities *Triennial Review Order* proceeding provided by the New Jersey Ratepayer Advocate concluded that Verizon failed to show "that there are any areas in New Jersey where the elimination of unbundled mass market switching would not impair CLECs."[88] The Ohio Consumers' Counsel concluded similarly based on the record developed in the Public Utilities Commission of Ohio's *Triennial Review Order* proceeding, noting that "there is impairment for unbundled local switching ("ULS") throughout the SBC Ohio ... and Cincinnati Bell Telephone Company territories."[89] The Ohio Consumers' Counsel further noted that " [i]f the Commission erroneously finds no

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86 *See Staff of the California Public Utilities Commission Report on Investigation Concerning Competitive Local Carriers' Deployment of Facilities,* WC Docket No. 04-313. CC Docket No. 01-338 at 8 (filed Oct. 4, 2004) ("California PUC Staff Comments").

87 *See Initial Comments and Waiver Request of the Michigan Public Service Commission*, WC Docket No. 04-313, CC Docket No. 01-338 at 5 (filed Oct. 4, 2004) ("Michigan PSC Comments"); *see also Comments of the New Jersey Division of the Ratepayer Advocate*, WC Docket No. 04-313, CC Docket No. 01-338 at 16 (filed Oct. 4, 2004) ("New Jersey Ratepayer Advocate Comments"); *Comments of the Office of the Ohio Consumers' Counsel on Notice of Proposed Rulemaking*, WC Docket No. 04-313, CC Docket No. 01-338 at 2 (filed Oct. 4, 2004) ("Ohio Consumers' Counsel Comments").

88 New Jersey Ratepayer Advocate Comments at 16.

89 Ohio Consumers' Counsel Comments at 2.

impairment for ULS where there is in fact impairment, then the ubiquitous UNE-P-based competition in SBC Ohio territory will be eliminated, and consumers will be harmed."[90] The Commission's national finding of impairment and unbundling obligation on the ILECs to provide local switching is substantiated by the state *Triennial Review Order* proceeding records that have now been made part of the record in this docket.

B. Impairment Is Pervasive Throughout The POTS Market.

The records developed in the state *Triennial Review Order* proceedings confirm the Commission's national finding of impairment with respect to unbundled access to the ILEC's local switch for mass market customers. CLECs seeking to compete against the ILEC in the POTS market continue to face substantial barriers to entry as a result of the ILEC's former monopoly in the POTS market. Costs and operational disparities associated with the ILECs' local network architecture make competing without unbundled access to the ILEC's switch nearly impossible eight years after the passage of the 1996 Act.

1. *The incumbency advantages of the ILECs still exist in the POTS market.*

Eight years after the passage of the 1996 Act, ILECs still enjoy the advantages of incumbency in the POTS market. No CLEC, regardless of how limitless its resources are, can duplicate the ILEC legacy network; deployment of the necessary facilities to do so would be both cost prohibitive and resource wasteful.[91] Even with unbundling in place, the ILECs still maintain a stronghold in the POTS market, providing service to over 151.8 million lines

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90 *Id.* at 7.

91 The Supreme Court noted as much when it concluded that "entrants may need to share some facilities that are very expensive to duplicate." *See Verizon Communications Inc. v. FCC*, 535 U.S. 467, 510 n. 27 (2002).

throughout the country or approximately 84% of the POTS lines available nationwide at the end of 2003.[92]

Even as CLECs self-deploy some of the essential facilities for providing service to the mass market, the ILECs continue to enjoy scale advantages over CLECs in provisioning and operating facilities to serve POTS customers. As the Commission noted in the *UNE Remand Order*, CLECs "encounter generally greater direct costs per subscriber when provisioning their own switches, particularly in the early stages of entry when [competitive] carriers may not have the large number of customers that is necessary to increase their switch utilization rates significantly."[93] The same holds true today. CLECs cannot attempt to overcome the scale advantages enjoyed by the ILECs and compete in the POTS market without access to unbundled local switching. There simply is no "functional equivalent" to the ILEC's switch for a new entrant in the mass market.

In the *Local Competition Order*, the Commission noted that the ILEC's legacy network "enables it to serve new customers at much lower incremental costs than a facilities-based entrant that must install its own switches, trunking and loops to service its customers."[94] The costs disparities inherent in the ILECs' legacy network continue today, despite the unbundling regime, and CLECs have not been able to substantially overcome the cost disparities

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92 *Local Telephone Competition: Status as of December 31, 2003*, Federal Communications Commission, Industry Analysis and Technology Division, Wireline Competition Bureau, Table 1 (rel. June 18, 2004) ("*2003 Local Telephone Competition Report*").

93 *Triennial Review Order* ¶ 260.

94 *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499, ¶ 10 (1996) ("*Local Competition Order*") (citing to *Local Competition NPRM* ¶ 6).

associated with competing against the ILEC in the POTS market. The USTA suggests that the Commission should disregard cost disparities between CLECs and ILECs in making its impairment determinations.[95] The Commission cannot do so, as barriers resulting from the ILECs' former monopoly, including the scale advantages enjoyed by the ILECs, continue to plague CLECs seeking to enter and compete in the POTS market. The costs of deploying facilities to replicate the ILEC's legacy network faced by CLECs are significant and in most cases prohibitive. The ILECs avoid these costs as a result of their historic monopoly status. These costs differences, which are "related to [the] structural impediments to competition" that the *USTA II* court found "relevant to the impairment analysis" cannot be ignored.[96]

BellSouth oversimplifies the analysis of cost disparities, concluding that once a competitive facility has been deployed, the cost disparities between the CLEC and the ILEC have been overcome, thus unbundling is no longer required.[97] This conclusion blatantly disregards the realities of competing against the ILEC in the POTS market. As the state impairment docket records show, even where CLECs have self-deployed switches, these switches are not being used to provide mass market services because CLECs cannot overcome the cost barriers that exist in serving mass market customers using UNE-L (including hot cuts, collocation, and transport costs associated with backhaul).[98]

Verizon is incorrect in its assertion that CLECs enjoy advantages over ILECs in the markets they attempt to serve, citing to disadvantages suffered by the ILECs for having to

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95 *See* USTA Comments at 10.

96 *USTA II*, 359 F.3d at 572.

97 *See* BellSouth Comments at 10.

98 *See* PACE Coalition *et al.* Comments at 66-81.

serve "under priced" residential customers.[99] Contrary to Verizon's contention, many CLECs do serve residential customers, adopting a "universal competitor" model of competitive entry.[100] Yet the "universal competitor" strategy is possible only because of the universal availability of unbundled local switching. With statewide availability, entrants are able to recover costs across low cost and high cost areas. If unbundled local switching were available only in high cost areas, the entry strategy would fail due to economic barriers to entry, including the costs associated with advertising the service over both urban and rural customer bases, the limited customer base growth available in rural areas, and high rural UNE loop rates.[101] Eliminate the CLEC's ability to serve the urban market with access to unbundled local switching for mass market customers and CLECs will not be able to serve smaller markets. The Commission cannot 'cherry pick' the markets where it wants competition to exist; it is the Commission's statutory obligation to promote competition for all customers across all geographic areas.

VI. THE GOALS OF THE 1996 ACT ARE NOT LIMITED TO ENCOURAGING FACILITIES-BASED COMPETITION

In its effort to bring the benefits of new technologies to a wider audience of users in all segments of society and geographic locales, Congress explicitly provided for three modes of competitive entry to the local telecommunications market: "the construction of new networks, the use of unbundled elements of the incumbent's network, and resale."[102] The Commission repeatedly has recognized that "there will be a continuing need for all three of the arrangements Congress set forth in Section 251 to remain available to competitors so that they can serve

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99 Verizon Comments at 11.

100 *See* PACE Coalition *et al.* Comments at 85-91.

101 *Id.* at Exhibit A.

102 *Local Competition Order* ¶ 12.

different types of customers in different geographic areas."[103] Acknowledging that some new entrants may "follow multiple paths of entry as market conditions and access to capital permit," the Commission properly has expressed no preference as to which entry method competitive carriers employed[104] and has correctly highlighted the importance of "ensure[ing] that all pro-competitive entry strategies may be explored."[105] The ILECs suggest that the Commission should now change its approach to focus exclusively on the promotion of "facilities-based" competition.[106] Such an approach would be inconsistent with the 1996 Act. The Commission is not free to sacrifice one method of entry identified by Congress in favor of another. It is fundamentally illogical to characterize the Act as favoring facilities-based entry when two of the three entry strategies embodied in the Act – unbundling and resale – were based on access to the ILEC network. It remains the Commission's statutory responsibility to ensure that all modes of competitive entry continue to be made available to CLECs.

A. Deployment Of Advanced Services Is One Of The Goals Of The 1996 Act And Has Not Been Sacrificed By The Unbundling Regime.

When Congress enacted the 1996 Act, its intent could not have been more clear: to encourage the deployment of advanced services and facilities *and* to bring competition to consumers of traditional phone services in the POTS market. In the years since the 1996 Act passed, these goals have not changed, nor have their importance. The Commission's unbundling policies must be designed to promote both; it is not free to merely encourage one, while ignoring

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103 *UNE Remand Order* ¶ 5 (citing *Local Competition Order* ¶ 12).

104 *Local Competition Order* ¶ 12.

105 *Id.*

106 *See* BellSouth Comments at 2; SBC Comments at 9; Qwest Comments at 11; USTA Comments at 8; Verizon Comments at 14.

the other. The twin goals of competition in the advanced services market and the traditional POTS market in no way conflict with one another and there is nothing in the directive of the court in *USTA II* that the Commission must conduct a "more nuanced" analysis of impairment that is "aimed at tracking relevant market characteristics and capturing significant variation"[107] that justifies the Commission ignoring the POTS market in favor of the advanced services or intermodal markets. The POTS market is a distinct and separate market from the advanced services market and the unique characteristics of the POTS market must be afforded the necessary considerations separate and apart from the advanced services market in determining impairment.

1. *The unbundling regime has not resulted in disincentives.*

The goals of advanced services deployment and POTS competition are not opposing. Opening the traditional POTS market to competition has created the necessary foundation for CLECs to enter the market and provide not only POTS services but also to deploy innovative services. The current unbundling regime, specifically unbundled access to the ILEC's switch, supports and encourages the deployment of advanced services, satisfying Congress's mandate while promoting POTS competition. In fact, figures reported by the Commission in its *Fourth Report to Congress*[108] demonstrate that while the current unbundling regime has been in place, the deployment of advanced services has tripled.[109] This growth and development has occurred in harmony with the on-going access by CLECs to the ILEC's switch. The unbundling

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107 *USTA II*, 359 F.3d at 563.

108 *Availability of Advanced Telecommunications Capability in the United States,* FCC 04-208, GN Docket No. 04-54, Fourth Report to Congress ("*Fourth Report to Congress*").

109 *Fourth Report to Congress* at 8.

regime has not resulted in disincentives for ILECs and CLECs "to engage in innovation, investment, and facilities-based competition" as Qwest would like the Commission to believe.[110] Maintaining the current unbundling regime and requiring ILECs to provide access to local switching to serve POTS customers does not to serve as a deterrent to the deployment and evolution of advanced services, but rather as a spur to its growth and deployment. The Commission need not sacrifice POTS competition for the deployment of advanced services.

VII. COMPETITION MUST NOT ONLY BE POSSIBLE BUT MUST ACTUALLY EXIST BEFORE A FINDING OF NON-IMPAIRMENT IS JUSTIFIED

The Commission cannot eliminate unbundled local switching from the list of network elements required to be unbundled on the basis of a finding that competition is technically possible in the POTS market. Rather, competitive alternatives to using the ILEC's switch must actually be in use before a non-impairment determinate can lawfully be made.

A. The Commission Cannot Extrapolate Competition From One Market To A Similarly Situated Market.

Any finding of non-impairment made by the Commission in this proceeding must be based on the actual conditions in the relevant market and not on hypothetical scenarios that may or may not be possible in the real world. It would be detrimental to POTS subscribers if the Commission were to adopt the approach proffered by the BOCs[111] and accept the hypothesis that if competition is viable in one market with certain characteristics, competition is a fortiori viable in other markets with similar characteristics. This claim is too far fetched to render an entire market not impaired solely on the basis that another market was able to sustain competition.

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110 Qwest Comments at 32.

111 *See* BellSouth Comments at 10; Qwest Comments at 19; SBC Comments at 30; Verizon Comments at 22-23.

Competition exists in markets under specific conditions. Certain of those conditions can be present in other markets and yet competition may not be viable for a litany of reasons. As stated by the *USTA II* court, competitive conditions in Market A are not irrelevant when deciding whether impairment exists in similar Market B; however, the existence of competition in Market A is not by itself "sufficient to establish competition" in Market B.[112]

B. The "Ability" To Compete Is Not Enough To Sustain A Finding of Non-Impairment – Actual Competition Must Be Present.

The "ability" to compete in the POTS market is not enough for the Commission to eliminate unbundling of the ILEC's local switch, as several commenters would like the Commission to believe.[113] POTS competition must actually be occurring before the Commission can even entertain making a finding of non-impairment in a market. The potential danger associated with equating "ability to" with "actual" competition is a premature non-impairment determination and the elimination of any choice in providers in the POTS market. In addition, a "choice" between the ILEC and one intermodal provider such as an ILEC-like cable company is not the competition envisioned by the 1996 Act.

Furthermore, notwithstanding BellSouth's claims, the mere existence of alternative switching facilities does not indicate that CLECs are "able" to compete in the POTS market without access to the ILEC's local switch.[114] The Commission's impairment analysis cannot be reduced to the idea that if there are third-party switches present, then there is non-impairment for the POTS market. The mere existence of competitive switching does not address

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112 *USTA II*, 359 F.3d at 575.

113 *See* BellSouth Comments at 13-14; SBC Comments at 29-30; Verizon Comments at 22.

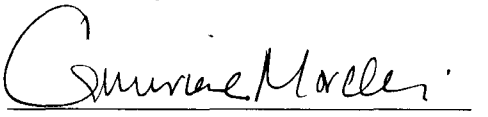
114 BellSouth Comments at 10.

whether those switches are being used to provide POTS services.[115] Mere deployment of a switch does not prove that competition is viable in the market; indeed, as discussed at length in the Joint Commenters' initial comments, the numerous other economic and operational barriers that exist today preclude those switches that have been deployed by CLECs from being used to serve the POTS market.[116]

VIII. CONCLUSION

For the foregoing reasons, the Joint Commenters respectfully request that the Commission grant the relief requested herein.

Respectfully Submitted,



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115 Clearly an impairment analysis that consists of a mere survey of where competitive switching is available would not satisfy the requirements of *USTA II* that the Commission perform a more "granular" and "nuanced" impairment analysis.

116 *See* PACE Coalition *et al.* Comments at 66-81.